Exam 1 – Version A

- Put your name on your scantron. Keep the cover sheet attached to this exam.
- Put your version (ex. Ver. A, see above) on your scantron under “Test No.”.
- Turn in both this exam (i.e. this question part) and your scantron. You are not allowed to take your exam with you.

1. Buck is President of Ozark Computer Consultants. The company employs 100 people all of whom are salaried (i.e. they are not paid by the hour). Buck decides to have a 1 hour meeting with all of the company’s employees once a week every week. Buck states: “The meeting will not cost the company anything more than the electricity to light and air condition the auditorium because the employees are salaried. I do not have to pay them anymore if they come to the meeting.” Assume the meetings do not hurt morale. Is Buck correct?
   a. No. The meetings will actually cost less than he says because the company will not have to light and air condition the employees’ offices when they are at the meeting.
   b. No. The employees could be engaging in other activities which would earn the company money instead of going to the meeting.
   c. Yes. The employees’ salaries are a fixed cost and cannot be changed in the short-run. When using marginal analysis, one should only look at what can be changed.
   d. Yes, but only assuming Buck is not ignoring any hidden explicit dollar costs such as money he has to pay to clean up the auditorium.

2. Which of the following best defines “supply” in economics?
   a. The sellers’ side of a market.
   b. Businesses.
   c. The $ volume bought and sold in the goods and services market.

3. Three managers of the Magic Potion Company are discussing a possible increase in production. Amy states; “We should examine whether or not productivity; output per worker, will rise or fall.” Bob states; “We should examine whether or not the extra revenue from selling the additional potions is greater than or smaller than the additional costs.“ Camillia states; “We should examine whether our average costs per unit of potion rises or falls.” Which managers advice best fits the principles taught in this course?
   a. Amy
   b. Bob
   c. Camillia
   d. None of the above. They are all economic boneheads.

4. You and your friend, Tracey Trekkie, are watching Star Trek one evening. Tracey states; “Today we use money to figure out or ration who gets what. With all that technology they (the people living in Star Trek’s time) have, there would be no need for money. Star Trek technology would mean that everyone can get everything they want and we would not need money or any other way to ration goods and services.” Tracey’s statement is:
   a. an example of reverse causation
   b. probably false. Human wants tend to always exceed our ability to meet those wants.
   c. true only if she excludes those in the bottom (approximately) half of Star Trek society.
   d. probably false. Technological advance is inevitably associated with more income inequality.
   e. both c & d
5. Brandon speculates in houses. He buys houses, often at auction, not for his own use. Instead, he buys houses only in hopes of selling them at a higher price than he paid. Brandon:
   a. is producing an externality
   b. is an example of local market power
   c. is engaging in a zero sum game
   d. is creating value

6. Romulus initially estimates that building and operating a hot dog stand at the state fair will cost him $4,000 (including the value of his time) and bring in $5,000 of revenues. He spends $3,000 on the hot dog stand, then realizes he erred. The hot dog stand is now almost certain to cost him a total of $6,000. Revenues are still almost certain to be $5,000. According to the principles taught in this class, should Romulus finish building the hot dog stand?
   a. Yes
   b. No

7. Which of the following is the most true?
   a. Markets generally do not encourage people to do good things for others. However, they are very good at encouraging people to do good things for themselves.
   b. Markets are the only way, yet discovered by humankind, to get people to do good things for others.
   c. While not the only way to get people to do good things for others, markets are usually quite effective and encouraging such behavior.

8. Al’s Shed Company (ASC) has the following costs based on the number of sheds he produces per month. For example, if he produces 0 sheds, his costs are $500 (rent, etc.). If he produces 3 sheds he pays $6,500 in costs. What is the marginal cost of producing the 4th shed?
   a. $32,000
   b. $8,000
   c. $2,000
   d. $1,500
   e. none of the above

<table>
<thead>
<tr>
<th>Sheds</th>
<th>Total Costs Incurred by ASC</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>$500</td>
</tr>
<tr>
<td>1</td>
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<tr>
<td>2</td>
<td>$4,500</td>
</tr>
<tr>
<td>3</td>
<td>$6,500</td>
</tr>
<tr>
<td>4</td>
<td>$8,000</td>
</tr>
<tr>
<td>5</td>
<td>$10,000</td>
</tr>
</tbody>
</table>

9. According to lecture, if there is only one cement company in a town, than company will:
   a. actually leave consumers as a group worse off than if there was no cement company.
   b. fail to create any value to consumers as a group. Consumers, on average, will be just as well off as if there was no cement company in town.
   c. create value for consumers as a group, but not as much as consumers would see if there were more than one cement company.
   d. create just as much value for consumers as they would see with more than one cement company.
   e. create more value for consumers then they would see with more than one cement company.

10. Mac owns a crop dusting company. Tosh owns several bee hives. One morning, while dusting someone else’s field, Mac accidentally sprays some Malathion (an insecticide) on Tosh’s hives. 40% of Tosh’s hives are destroyed. Tosh never learns how this happened. This is an example of:
   a. why some economists argue for the “Invisible Hand” of government to intervene in markets.
   b. an externality
   c. “ceteris paribus”, or “buyer beware”.
   d. the “post hoc, ergo protor hoc” fallacy.
   e. what economists consider a sad, but wholly unavoidable, side effect of progress.
11. Bobby Buyer just purchased a used motorcycle from Sheldon Seller. Sheldon owned the motorcycle for 5 years. Bobby paid $1,200 for the motorcycle. The motorcycle is worth at least $1,500 to Bobby. He would have been willing to pay up to $1,500. Which of the following is most likely true of Sheldon Seller?
   a. Sheldon most likely gained from the sale.
   b. Sheldon most likely lost from the sale.
   c. Sheldon had to be basing his decisions on erroneous information.
   d. both b and c
   e. none of the above

12. Assume that women are more likely to receive professional training than in the past. Unlike the past, Afghan women are now almost as likely to have a degree or other type of training as men. What, according to the principles discussed in class, is likely to happen to Afghan birthrates?
   a. They will likely decrease. Fewer births per family will likely be seen.
   b. They will likely be unchanged. The same number of births per family will likely be seen.
   c. They will likely increase. More births per family will likely be seen.

13. According to the Fort Worth Star Telegram article we read, what is happening to the average family size of Latinos families in the United States? Why is the likely reason for this according to the article?
   a. U.S. Latino family size in falling. This is likely because a growing percentage of Latino families now classify themselves as protestant. Unlike the Catholic Church, many protestant churches condone birth control.
   b. U.S. Latino family size in falling. This is likely because more U.S. Latino families now have both spouses working outside of the home.
   c. U.S. Latino family size in rising. This is likely because Latinos in the U.S. earn more than Latinos in other nations. U.S. Latinos can afford to have more kids.
   d. U.S. Latino family size in rising. This is likely because a growing percentage of Latinos in the U.S. are adopting U.S. “mid-western” culture.

14. Which of the following is not a “factor of production” as defined in economics?
   a. a seam of iron ore just under the surface in northern Minnesota
   b. Brenda, a worker with a degree in computer science and 6 years professional experience
   c. a machine which can stamp out 120 metal car doors per hour.
   d. $1,500,000 raised by 4 Monkeys, Inc. through the sale of their company’s stock.
   e. all of the above are “factors of production” as defined in economics

15. Who first described the concept of comparative advantage?
   a. John Adams
   b. John Locke
   c. Deirdre McCloskey
   d. David Ricardo
   e. Adam Smith

16. Who coined the term “Invisible Hand”?
   a. John Adams
   b. John Locke
   c. Deirdre McCloskey
   d. David Ricardo
   e. Adam Smith
17. In what book was the term “Invisible Hand” first used?
   a. Gains from Trade among Nations  
   b. National Interest, Self Interest  
   c. The Political Economy of Trade  
   d. Trade and Prosperity  
   e. The Wealth of Nations

18. Given the information below, what is the amount of income created in this economy?
   Total Sales of Final Goods & Services (revenues of firms): $18 Trillion
   Wages: $10 Trillion  
   Rent: $2 Trillion  
   Interest: $3 Trillion
   a. $33 Trillion  
   b. $18 Trillion  
   c. $15 Trillion  
   d. $10 Trillion  
   e. none of the above

19. Which of the following best defines “ceteris paribus.”
   a. Most causation chains have “feedback effects”. An increase in X (ex. productivity) may change Y (ex. spending), and the change in Y causes X to change more, which changes Y, etc.
   b. What is true for the individual may not be true for the group as a whole.
   c. Nothing changes except one specified thing.
   d. When dealing with large numbers, group tendencies offset any individual variations.
   e. “Constant change”. Theories should not assume the world is a static, unchanging, place.

20. Which of the following best illustrate the idea of the “Invisible Hand”.
   a. Gibbons Medical Inc. (GMI) is a for profit firm. It invents a vaccine for the common cold and earns billions in profits. People gladly buy the vaccine, but resent GMI’s profits.
   b. Most causation chains have “feedback effects”. An increase in X (ex. productivity) may change Y (ex. spending), and the change in Y causes X to change more, which changes Y, etc.
   c. Simply asking people may not be accurate measure of what motivates them. Observing their actions is a better way to determine their true motivations.
   d. When dealing with large numbers, group tendencies offset any individual variations.
   e. The pursuit of money can be altruistic. Although it is not commonly perceived, a large percent of income earned goes to charity.

21. Consider the PPC at right. What happens to the opportunity costs per added tank as the production of tank increases?
   a. the opportunity cost per added tank decreases.
   b. the opportunity cost per added tank increases.
   c. The opportunity cost per added tank could increase, stay the same, or decrease depending whether the PPF shifts in, out, or stays in place.
   d. the opportunity cost per added tank remains constant.

22. Consider the following statement. “If the federal government spends $200 billion on Hurricane Katrina recovery efforts without either raising taxes or cutting other government spending, the increased government borrowing will drive up interest rates an average of 0.5%”. This statement is:
   a. normative  
   b. oviparous  
   c. oviparous  
   d. positive  
   e. viviparous
23. Consider the following statement. “Spending on national defense should be cut to pay for Hurricane Katrina recovery efforts. It is better to take care of those at home before worrying about what is happening abroad.” This statement is:
   a. normative  
   b. oviparous  
   c. oviparous  
   d. positive  
   e. viviparous

   Use the following diagrams to answer #s 24 – 27. You may use any option as many or as few times as you wish.

24. During the middle 1990’s the U.S. unemployment rate remained roughly constant. Other measures such as office space vacancies also remained relatively constant. At the same time, production in the U.S. increased greatly. Which of the above graphs best illustrate this?

25. It’s 2010 and Japan’s economy is recovering from a recession. Its unemployment rate falls rapidly. Which of the above graphs best illustrate this?

26. President Eisenhower once stated; “Every gun that is made, every bomb and missile, signifies a theft from those who are not fed.” Which of the above graphs best illustrate this?

27. President Roosevelt’s 1933 inaugural speech came while the United States was in the Great Depression. In response to the vast number of unemployed workers, Roosevelt declared; “our primary task is to put people to work!” Which of the above graphs best illustrate this goal?

28. Which of the following is an argument for free(r) trade?
   a. Trade is the best way to protect workers in industries having trouble competing in foreign markets.
   b. Trade may allow companies to achieve large-scale production and thereby reduce costs per unit.
   c. Trade reduces a nation’s dependence on foreign suppliers of critical military parts and hardware.
   d. Trade encourages a nation towards greater self-sufficiency.
   e. both a & d
29. In 1939 the U.S. economy still had not completely recovered from the Great Depression. In 1966 the U.S. economy was booming. Production was high and unemployment was low. In both years, the U.S. began a large military build-up (one in response to conflict in Europe and China and the other in response to conflict in Vietnam). Assume the military build-up is the same relative size in both cases (say 8% of GDP). In which case would production of non-military goods (i.e. civilian goods) be most likely to fall?
   a. The 1939 build-up  b. the 1966 build-up

30. Robinson and Friday are trapped on a desert island. They live on fish and pineapples. Friday is a much, much better fisherman than Robinson. Friday is also slightly better at gathering pineapples than Robinson. According to the principles learned in class:
   a. Friday can gain from trade, but Robinson cannot.
   b. Robinson can gain from trade, but Friday cannot.
   c. Both can gain from trade, but only if Friday does more work and values the well-being of Robinson.
   d. Both can gain from trade if Friday specializes in fish, and Robinson specializes in pineapples.
   e. Both can gain from trade if Friday specializes in pineapples, and Robinson specializes in fish.

31. In class, it was suggested that the European might be using a method to make international competition between Europe’s Airbus and America’s Boeing less “free”. What was this method?
   a. Government subsidies provided to Airbus.
   b. Tariffs on Boeing airplanes sold to European airlines.
   c. A quota limiting the number, or more precisely the seating capacity, of Boeing airplanes that can be sold in Europe each year.
   d. Not recognizing U.S. aviation patents (allowing Airbus to use Boeing innovations royalty free).

#’s 32 – 33: Assume that between 2005 and 2025, productivity in all industries in the U.S. increases by 25% while productivity in all industries in Europe increase by 50%.

32. Which of the following will likely happen to living standards in the U.S.?
   a. Material standards of living in the U.S. will fall. The average American will have fewer material goods and services.
   b. Material standards of living in the U.S. could either rise or fall depending on how many industries the U.S. loses.
   c. Material standards of living in the U.S. will rise. The average American will have more material goods and services.

33. Will the U.S. still be able to compete; i.e. export goods and services to Europe?
   a. No.
   b. Yes.
   c. Yes, but only if the U.S. government uses tax dollars to provide export subsidies.

34. Compared to Mexico, the U.S. has 85% higher productivity in grape production, and 25% higher productivity in tomato production. Assume there are no other goods which can be traded and no other countries with which to trade (i.e. assume a 2-good, 2-country world). The U.S. will likely:
   a. export both grapes and tomatoes to Mexico.
   b. export grapes to Mexico, and import tomatoes from Mexico.
   c. import grapes from, and export tomatoes to, Mexico.
   d. import both grapes and tomatoes from Mexico.
   e. information on absolute costs is needed to answer this question.
35. Consider the following statement. “Study after study clearly indicates that Canada is a richer nation because of its trade with the United States. Since Canada is benefiting so much from trade with the U.S., the United States must be getting the raw end of the deal. The U.S. must be losing from trade with Canada. It is time for our government to raise tariffs on Canadian goods coming into the U.S.” This statement is likely:
   a. False. While the U.S. is likely seeing lower living standards as a result of free trade with Canada, raising tariffs would likely damage the defense relationship the U.S. has with Canada.
   b. False. The U.S. is likely experiencing higher living standards as a result of its trade with Canada.
   c. True. The U.S. is likely seeing lower living standards as a result of free trade with Canada. Tariffs would mean less trade with Canada and more revenue for the U.S. government.

Use the following chart to answers #’s 36 - 39.

<table>
<thead>
<tr>
<th>Country</th>
<th>Beef</th>
<th>Honey</th>
</tr>
</thead>
<tbody>
<tr>
<td>Babylon</td>
<td>12 hours</td>
<td>4 hours</td>
</tr>
<tr>
<td>Persia</td>
<td>6 hours</td>
<td>3 hours</td>
</tr>
</tbody>
</table>

36. In order to gain from trade, which good or goods should Persia specialize in?
   a. both honey and beef  
   b. honey  
   c. beef  
   d. neither honey or beef

37. Which nation has the highest productivity in beef?
   a. Babylon  
   b. Persia  
   c. More information is needed to answer this.

38. True or False: Both nations can gain from trade if Honey and Beef are traded at a rate of: 4 Honey : 1 Beef.
   a. True  
   b. False

39. True or False: Both nations can gain from trade if Honey and Beef are traded at a rate of 2.5 Honey : 1 Beef.
   a. True  
   b. False

40. In the article “Other Things Equal: Learning to Love Globalization”, Deirdre McCloskey argues that free trade:
   a. is one of the better ways to increase living standards in the less developed world.
   b. while it immediately benefits peoples of the world on average, is bad for workers in less developed nations.
   c. while it will in the long-run benefit peoples of the world, in the short-run it is almost entirely bad for industrial workers in less developed nations. Gains to less developed nations will not be seen for a generation or two.
   d. Americans giving more to foreign charities while giving less to domestic (American) charities.
Answer #s 41 – 45 based on the PPFs below. Assume Egypt is the only nation with which Kush can trade, and vice versa. Further, assume Sorghum and Wheat are the only two goods. Finally, assume goods can be shipped freely.

41. Which good or goods does Egypt have a comparative advantage in?
   a. both sorghum and wheat
   b. sorghum
   c. wheat
   d. neither sorghum or wheat
   e. information on absolute costs is needed to answer this question.

42. True or False: Both nations can gain if the goods are traded at a rate of: 5 Sorghum : 1 Wheat.
   a. True
   b. False

43. True or False: The following represents a feasible trade which will allow both nations to gain.
   Egypt: Exports = 480 Sorghum, Imports = 80 Wheat.
   Kush: Exports = 80 Wheat, Imports = 480 Sorghum
   a. True (both gain)
   b. False
   c. Information on absolute costs and available labor is needed to answer this question.

44. True or False: The following represents a feasible trade which will allow both nations to gain.
   Egypt: Exports = 70 Wheat, Imports = 420 Sorghum
   Kush: Exports = 420 Sorghum, Imports = 70 Wheat
   a. True (both gain)
   b. False
   c. Information on absolute costs and available labor is needed to answer this question.

45. True or False: The following represents a feasible trade which will allow both nations to gain.
   Egypt: Exports = 400 Sorghum, Imports = 100 Wheat.
   Kush: Exports = 100 Wheat, Imports = 400 Sorghum
   a. True (both gain)
   b. False
   c. Information on absolute costs and available labor is needed to answer this question.